

Plain Language – The Benefits to Small Business

Testimony of

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Chairman Braley, Ranking Member Davis, and Members of the Subcommittee:

Thank you for inviting me to testify today. I should say at the outset, as is traditional, that my testimony today is on my own behalf as Chairman of the SEC, and does not necessarily represent the views of the Commission or individual Commissioners.

I am delighted you're focused on this topic. As the champions of small business in the Congress, you have hit the jackpot in focusing on the importance of using plain language in government rules, regulations, and paperwork. The time and money that is wasted on translating legalese into plain English is dead weight economic loss. It benefits no one, and harms millions of consumers who pay for it.

Of course, while you are leaders in this effort, you are not the first mavericks in Congress to take up the battle for clearly written legal rules. In fact, the very first reported appearance of the word “gobbledygook” was in 1944, when it was coined by a Congressman actually named Maverick. U.S. Representative Maury Maverick was a Texas Democrat who wrote a memo that banned all “gobbledygook language” from his office. He said he made up the word to imitate the noise a turkey makes. And to show you just how serious he was about plain English, he added in his memo, “Anyone using the words ‘activation’ or ‘implementation’ will be shot.”

At the SEC, we have more modest penalties in store for both staff and public offenders. But we're dead serious about plain English. That's because it's our job to be the investor's advocate, and investors deserve concise and clearly written disclosure that helps them quickly focus on what's important in making financial decisions. Using plain English respects the fact that investors are busy people, and lets them use their time more productively. Clearly presented information also makes investment analysts and every other market actor more efficient. It improves the process of price discovery on our securities exchanges. And by exposing the financial doings of public companies to more direct sunlight, it makes our markets more honest – strengthening investor confidence.

The SEC has many plain English initiatives underway. Our plain English requirements now apply to both offering documents and periodic reporting by public companies. They apply to mutual fund disclosure, which benefits millions of ordinary Americans. And they apply to our own communications to the public.

It's a sad truth that our government's laws and rules are not only mostly written by lawyers, but they seem also to be written primarily for the benefit of other lawyers. This makes compliance with the laws more expensive, because people who have to follow the laws and rules need to hire lawyers to find out what they mean. But legalese does more than waste time and money. When laws and rules are hard to understand, it's more likely that people who are trying to comply won't be able to do so, because they don't fully understand what's being asked of them. So the government gets less of the behavior that it wants; the people trying to be good and do what government wants get frustrated and angry; our economy is less efficient because of all the expense involved; and overall, confidence in government is eroded, because when the poorly written laws and rules are enforced, people view it as unfair and arbitrary.

Clarity in spelling out a citizen's obligations is one of the fundamental requirements of the rule of law. When Hammurabi erected his stone tablets in the city square of Babylon 3800 years ago, civilization made a great advance. From that moment forward, the law was no longer arbitrary. For the first time, citizens could know in advance the standard to which they should conform their conduct. That is the difference between the rule of law and the rule of men.

In our own time, when we highly prize the rule of law, we face the same risk as our ancient forebears, but for a different reason. All of our laws are written down — thousands of pages of them. But there are now so many laws and rules, and they are so hard to understand, that once again it's becoming hard for citizens to know in advance the rules by which they should arrange their lives and their business affairs.

And it isn't just the hundreds of thousands of pages of law and regulations that are responsible for this. Beyond the legal text there is an ever-growing case law that is necessary to interpret poorly written statutes and regulations. Not surprisingly, this often produces competing interpretations of the many grey areas. The result is a 21st century version of pre-Hammurabian days, when the law was arbitrary because no one really understood what it was.

There is nowhere that certainty in the law is more important than in small business. Each day, every small business executes make-or-break choices that depend on knowing in advance what the legal rules are. The small business people who are working hard each day to create the goods and services that their communities demand need to know how to navigate in a sea of regulation. We owe it to them to provide a clear answer.

At the SEC, we're taking plain English to the next level. In addition to using plain language in our writing, we're directly helping people to understanding our rules, and the laws we administer. As one part of this effort, we've published the SEC's own "Plain English Handbook."

Another area in which we're reaching out to help small business understand our rules is in the investment advisory industry. This is one of the fastest growing segments of the securities

industry for small business. In the past three years, almost 4,000 new advisers registered with the SEC for the first time. Obviously, both these small businesses and the people they're advising have a strong interest in seeing to it that their job is done right. But our experience has shown that newly-registered firms may not be familiar with what's required of them under the Investment Advisers Act. And they probably don't fully understand their compliance obligations under its key provisions.

Since the first step in understanding your compliance obligations is to know what the law says, we've actually "translated" the key provisions of the Investment Advisers Act into plain English. Last summer, we delivered this plain English summary of the law to new investment advisers by email. And we added a "welcome" letter listing all of the other resources we make available to help with understanding our rules. We also put this information up on our public website.

One of the best features of the new plain-English translation of the Investment Advisers Act is that each plain English description is hyperlinked to the actual text of the law. So it's easy to click back and forth to fully understand what a particular provision of the law means. Because we've gotten such positive feedback from our newly registered investment advisers, just yesterday we emailed the plain English translation of the Advisers Act to all investment advisers who have registered with the SEC in the last six months – more than 500 new firms.

We're also working hard to ensure that the materials publicly registered companies provide to investors are readable and understandable. If we were to look at the SEC as a business, one of its most important product lines would be disclosure documents. After all, it's our rules that result in the proxy statements and the annual reports that companies mail to investors across the country. The reason we're in this business is that we firmly believe informed investors will make better choices.

But in order for investors to make better choices based on full disclosure, they have to read it. If investors can't read and understand the disclosure documents – if instead, they just throw out the proxy statement or the annual report when it comes in the mail because they don't have the time to fight with the legalese – then the entire purpose is defeated. We have some empirical evidence that in fact, most retail investors are throwing away the disclosure documents that the SEC requires, instead of reading them.

When your customers routinely throw your product away, you've got a problem. There can be many reasons that our customers might be dissatisfied, but the most obvious is that investors are busy people. Wading through dense legalese isn't their day job, and they ordinarily just don't have time for it. If time is money, then poorly written disclosure documents are wasting one of the investor's most important assets.

At the SEC, we've noticed that public companies take a great deal of care in sprucing up their catalogs and sales materials so customers will be interested in buying their products. Doesn't it make sense that they – and we, the government – should take the same degree of care in making investor materials readable?

Our plain English efforts are focused on the areas where consumers have the most to gain. For retail investors including many small businesses, that means mutual funds – where nearly half of the more than \$3 trillion that Americans have in 401(k) plans and other defined contribution plans is invested. That's why, just a few months ago, the Commission proposed rule changes to make mutual fund disclosure easier to understand. The key innovation is a new summary prospectus, which would give all mutual fund investors a clear, concise description of the key information they need to make an informed investment decision.

Under this proposal, every mutual fund would include key information in plain English at the front of the mutual fund prospectus. Like the risk/return summary that is already required at the front of every mutual fund prospectus, this summary would include a fund's investment objectives and its strategies, risks, and costs. It also would include brief information regarding top ten portfolio holdings, investment advisers and portfolio managers, purchase and sale procedures and tax consequences, and how the people who sell the fund are paid. The rule changes would also encourage funds to exploit the Internet's capacity to allow investors to choose the way they view more detailed information. This will make reading a mutual fund prospectus far easier than it is today. And by standardizing the presentation of the essential information, the proposed rules intend to make comparing mutual fund information easier. We hope to have the final rules in place by late summer.

Yet another example of how we're using plain English to help individuals and small business is our proposed new rules to improve the quality of disclosure that investors receive about their investment advisers. The rules we proposed two weeks ago would require investment advisers to give clients a brochure written in plain English. The brochure would also be available on the SEC-sponsored Investment Adviser Public Disclosure web site. It would offer investors clearly presented information about an investment adviser's business practices, conflicts of interest, and disciplinary history.

One further area where we're working to promote clarity is our new executive compensation disclosure regime. In the past, executive compensation was among the most complicated subjects for investors to sort out. And it presented some of the biggest challenges when it came to analyzing and comparing data. To address this problem, the Commission recently enacted new rules aimed at letting investors see clearly how the executives who work for them are paid.

An important feature of the new rules is the narrative discussion of the company's compensation policies. The Compensation Discussion and Analysis offers an opportunity for the company to cast aside the boilerplate, and explain to the shareholders the how and why of its approach to executive pay. This helps provide context for the numbers in the tables that follow it. The new rules explicitly require that the narrative be written in plain English.

Mr. Chairman, these are just some of the many ways that the SEC is working to promote plain English to make life better for investors, for companies large and small, and for our markets. But I also want to congratulate you and this subcommittee for your focus on the importance of plain language across the entire government. And in particular, I appreciate your interest in legislation such as H.R. 3548, the *Plain Language in Government Communications Act of 2007*, which was authored by Chairman Braley. As you know there are similar efforts

underway in the Senate, led by Senator Akaka who has introduced S. 2291. I am certain that small business would welcome a law that establishes plain language as the standard style of communication for federal documents issued to the public. It's heartening that the House bill has already been unanimously approved by the House Oversight and Government Reform Subcommittee on Information Policy, Census, and National Archives.

Your bill, Mr. Chairman, would require the use of plain language in any new or revised document issued by a federal agency. That is certainly a good start. I note that the bill would cover any documents that explain how to obtain a benefit or service, including letters, forms, notices, and instructions. The next step, of course, would be to include regulations. I am certain there are reasons for that modesty in the bill's objective. But I encourage the members of this Committee to aggressively pursue the goal of plain language in regulations as well. I have been fighting for this at the SEC, but as you may see from our most recent proposed rules, legalese in rule text remains alive and well even at our agency.

Finally, I would point out that the key to achieving real change in increasing the use of plain language is the adoption of objective standards for measuring whether government writing is in fact understandable. Fortunately, there is useful experience in the states that can guide us in doing this. Thirty-five states have already enacted plain language laws, and many of them have been quite successful in eliminating gobbledeygook from consumer sales documents and insurance contracts. For example, Pennsylvania's Plain Language Consumer Contract Act includes specific tests of what plain language is, and penalties for non-compliance. But Pennsylvania's admirable law also shows the need for federal action, because it excludes language intended to comply with federal requirements.

What we don't need, of course, is a new bureaucracy of plain language police in every agency, wasting the taxpayer's money. What we do need is clearer writing – and there are easy-to-use tools that every federal worker already has at his or her own desk. In Microsoft Word, for example, you can easily subject your own writing to the Flesch-Kincaid readability algorithm. It's a feature included under the Spelling and Grammar options that can be set to pop up automatically when you use the spell check tool. Word will show both the Flesch Reading Ease score and the Flesch Grade Level.

Interestingly, this test – which was developed at Columbia University – was created by a lawyer who was also a writer by training, and he earned his Ph.D. for inventing it. The algorithm computes readability based on the complexity of the words used. Specifically, it measures the average number of syllables per word, and the average number of words per sentence.

Scores on the test range from 0 to 100. Just as in English class, getting 100 is good. The higher the score, the more readable the writing. To provide a little context, what the test administrators consider "standard writing" – the kind, for example, that appears in Readers Digest – averages about 60 to 70 on this scale. Most states that have plain English standards in force for insurance forms require a score between 40 and 50 on this test. My testimony today scores just under 49.

Sadly, in an independent review of proxy statements conducted last year, the average description of how much the company's executives were paid received a Flesch Reading Ease

score of just 34.86. If that were your grade in English class on a 100-point scale, you'd not only flunk - you'd be sent back a grade.

When compliance with government rules gives rise to this kind of writing, everyone is worse off – especially the people who are supposed to be able to read it. Fully two-thirds of American adults simply can't read at a level of 34.86, according to the Accessibility Institute at the University of Texas.

Of course, readability tests such as Flesch-Kincaid or another popular metric, the Gunning-Fog Index, are only a rough guide. Like the grammar check in Microsoft Word, they wouldn't recognize poetry if they saw it. They certainly can't tell if the proxy statement disclosures are accurate and complete, which is what the whole enterprise is ultimately about. Even Rudolf Flesch, who created the system, was worried that some people would misuse his “simple yardstick” by taking it too seriously and viewing it as more than a rough estimate.

On the other hand, these are laws, regulations, government documents, and investor communications we're talking about. It's not supposed to be Hemingway. So if we lose the capacity for poetry in the process of keeping things clear and understandable, that's a price we should happily pay.

But far better than any mathematical formula for measuring readability is testing a document on real people. That's why the SEC is planning to measure the effects of our efforts by talking to real investors.

Under the leadership of Kristi Kaepplein, the Director of the SEC's Office of Investor Education and Advocacy, the SEC will soon conduct a baseline survey of America's investors to find out whether they find proxy statements, 10-Ks, and other SEC-required disclosure documents to be useful – and if not, why not. The survey will also gather ideas on what would make these documents more useful. One of the questions we will ask is this: when your proxy statement or mutual fund prospectus comes in the mail, do you spend more than three minutes reading it? Or do you just throw it away? Periodically, we will go back into the field and ask that question again. Over time, we hope to see a significant decline in the percentage of investors who routinely put SEC documents in the trash.

Mr. Chairman, the attention that you and your fellow Committee members are paying to this important subject is long overdue. Eliminating waste in government is an objective that everyone shares in theory, but it always seems difficult to find good opportunities. Here is an outstanding opportunity to achieve enormous savings for both small business and consumers without any countervailing loss of a government interest. In fact, the government interest is advanced as well by eliminating legalese in government writing, because when it's easier to understand the rules, more people will follow them.

Thank you for inviting me to testify. I am happy to answer any questions.